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IN THE

Supreme Court of the United States

OCTOBER TERM, 1940

WRIGHT MORROW, *Petitioner*,

vs.

FRANK SCOFIELD, Collector of Internal Revenue,
Respondent.

Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit.

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Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit.

Wright Morrow prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Fifth Circuit entered in the above entitled cause on December 12, 1940, affirming a judgment of the United States District Court for the Western District of Texas.

OPINIONS BELOW

The District Court delivered no opinion. The opinion of the Circuit Court of Appeals (R. 59) is reported at 116 Fed. (2d) 17.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered December 12, 1940 (R. 65). On December 27, 1940, a Judge of the Circuit Court of Appeals granted Petitioner's motion to extend until January 16, 1941, the time for filing a motion for rehearing (R. 67). The Motion for Rehearing, filed on January 15, 1941, was denied without opinion on February 1, 1941 (R. 74). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

The documentary stamp tax title of the Revenue Act of 1926, as amended, requires the affixing of stamps to documents effectuating sales of lands, tenements or other realty.

The first question presented is whether the incidence of this tax is governed by the law of the State where the property is situated, so that Petitioner's assignments of oil and gas leases on lands in Texas must bear stamps, while identical assignments of leaseholds on lands in certain other states are not taxed; or is the incidence of the tax to be governed by federal or general law under which oil and gas leases and assignments thereof are not sales of lands, tenements or other realty.

If State law does govern the incidence of the tax, then are Section 800 and Schedule A-8 of the Revenue Act of 1926 (as amended) as applied in this case, unconstitutional and invalid because they levy an excise

tax which is not geographically uniform, as required by Article 1, Section VIII, Clause 1 of the Constitution of the United States?

STATUTES AND REGULATIONS

The controlling language of Section 800 and Schedule A-8 of Title VIII of the Revenue Act of 1926, as amended by Section 725 of the Revenue Act of 1932, is as follows:

> "Sec. 800. * * * there shall be levied, collected, and paid, for and in respect of the several * * * documents, instruments, matters, and things mentioned and described in Schedule A of this title, * * * the several taxes specified in such schedule. * * * "
>
> "8. Conveyances: Deed, instrument, or writing, * * * whereby any lands, tenements, or other realty sold shall be granted, assigned, transferred, or otherwise conveyed to, or vested in, the purchaser or purchasers, or any other person or persons, by his, her, or their direction. * * * "

These sections of the statute, as well as pertinent Treasury Regulations and rulings are set out in full in the Appendix, pages 17 to 18, infra.

STATEMENT

On July 31, 1935, Petitioner assigned to Stanolind Oil & Gas Company various oil and gas leaseholds covering lands in Texas and Louisiana for $19,717,500 and $2,125,039, respectively (R. 28). All of the leaseholds assigned were held under ordinary commercial

oil and gas leases, and it was stipulated that all leases and assignments, both as to Texas and Louisiana lands, were identical.[1]

Long continued Treasury Regulations construing Section 800, Schedule A-8 of the Revenue Act of 1926, as amended, (and the same language in earlier Acts) had provided that what constituted "lands, tenements and other realty" within the purview of the statute was to be determined by the law of the State in which the property was situated.[2] Carrying this out, it had been specifically ruled that oil and gas leases and assignments thereof covering lands in Texas should bear stamps,[3] while those on lands in Louisiana should not.[4]

To comply with these rulings, Petitioner purchased from Respondent, and affixed to the Texas assign-

[1]A specimen oil and gas lease and an assignment were attached to the stipulated facts (Exhibits A and B) as being typical of all such leases and assignments (R. 28, 31, 12 and 17).

[2]Regulations 71 was promulgated to enforce the stamp tax provisions of the Revenue Act of 1932. Article 84 thereof reads, "What constitutes 'lands, tenements and other realty' is determinable by the law of the State in which the property is situated." A short history of Section 800, Schedule A-8 of the Revenue Act of 1926, as amended by the Revenue Act of 1932, its predecessors and the earlier applicable Regulations will be found in the Appendix, p. 18.

[3]S. T. 868, 1937-2, C. B. 527. See Appendix, p. 19; See also, S. M. 4439, IV-2 C. B. 52.

[4]G. C. M. 913, V-2, C. B. p. 255. See Appendix, p. 21. By Act 205, approved July 5, 1938, the Louisiana Legislature provided, in effect, that oil and gas were real property subject to ownership in place; whereupon the Bureau ruled that oil and gas leases in Louisiana lands, executed after July 5, 1938, were subject to the documentary stamp tax; those executed prior to that date are exempt. G. C. M. 22,132, I. R. B. No. 27 (July 1, 1940), p. 23. See Appendix, p. 23.

ments, stamps in the amount of $19,715.50, but he affixed no stamps to the Louisiana assignments (R. 30).

Petitioner duly brought suit to enforce payment of a proper claim for the refund of the amount so paid for the stamps (R. 1). The trial court denied recovery (R. 47), and this decision was affirmed by the Fifth Circuit Court of Appeals (R. 65).

SPECIFICATION OF ERRORS TO BE URGED

1. The Circuit Court of Appeals erred in holding that the instruments by which Petitioner assigned oil and gas leaseholds covering lands in Texas were subject to the tax imposed by Section 800 and Schedule A-8 of Title VIII of the Revenue Act of 1926, as amended by Section 725 of the Revenue Act of 1932.

2. The Circuit Court of Appeals erred in holding that such taxing statutes—which, *in terms*, impose a tax upon any instrument "whereby any lands, tenements or other realty sold shall be granted, assigned, transferred or otherwise conveyed"—impose a tax upon any instrument which, in substance, transfers interests in realty.

3. The Circuit Court of Appeals erred in holding that Texas law should be applied in determining whether the assignments in question were subject to the tax, and in failing to construe such stamp tax statutes so as to give a uniform application to a nationwide scheme of taxation.

4. If Section 800 and Schedule A-8, Title VIII of the Revenue Act of 1926, as amended, require that the

incidence of the tax imposed thereby be determind by State law, then the Circuit Court of Appeals erred in failing to hold such statutes, as here applied, unconstitutional and invalid, in that they levy an excise tax which is not geographically uniform, as required by Article 1, Section VIII, Clause 1 of the Constitution of the United States.

REASONS FOR GRANTING THE WRIT

The writ should be granted because the holding of the Court below conflicts with controlling decisions by this Court and with applicable decisions by other Circuit Courts of Appeal, and because the Court below decided an important question of federal law which has not been, but which should be, decided by this Court.

The opinion below (R. 59) is confusing and somewhat contradictory and the conflicts relied upon here will more clearly appear after an analysis of that opinion.

In ascertaining whether the statute applied to petitioner's transactions, only three questions were or could be presented for determination:[5]

(1) Was there a sale?

(2) Was the thing sold lands, tenements or other realty?

(3) Are questions 1 and 2 to be decided by refer-

[5]The controlling parts of Sec. 800, Schedule A-8 of the Revenue Act of 1926, as amended, are: "* * * deed, instrument or writing * * * whereby any lands, tenements or other realty sold shall be * * * conveyed. * * *"

ence to the law of the State where the property is situated, or by federal rule?

The taxing authorities clearly took the position that, since by the laws of Texas an oil and gas lease was the conveyance of land for an undeterminable period of time,[6] the Act applied, and they have consistently held that where State law is otherwise as to the interest conveyed by an oil and gas lease, the Act does not apply.[7] The authorities are clear that under federal or general law an oil and gas lease is not a conveyance of land.[8] Therefore by affirming a decision in favor of the Respondent on the merits, the Court below must necessarily have held that the law of Texas controlled the incidence of the tax, and that there had been a sale of lands, tenements or other realty. This is true even though parts of the opinion below may appear to state

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[6]Letter rejecting claim for refund (R. 45).

[7]The more important of the rulings are summarized in the Appendix, page 27. States where oil and gas leases are not subjected to the documentary stamp taxes provided by Schedule A-8 are Kansas, Oklahoma, West Virginia, and Louisiana (leases executed prior to July 5, 1938).

[8]Burnet v. Harmel, 287 U. S. 103; Ohio Oil Company v. Indiana, 177 U. S. 190; Walls v. Midland Carbon Company, 254 U. S. 300; West v. Kansas Natural Gas Company, 221 U. S. 229. The Bureau has recognized that under the federal rule an oil and gas lease is not a conveyance of realty. G. C. M. 913, V-2, C. B. 225, set out in Appendix, p. 21. In Burnet v. Harmel this Court said: "By virtue of the lease, the lessee acquires the privilege of exploiting the land for the production of oil and gas for a prescribed period; he may explore, drill, and produce oil and gas if found. * * * Thus tested, we find in the Texas leases no differences from those leases where the title to the oil and gas passes only on severance by the lessee. * * *."

that State law is not controlling, or that it is controlling only when, in the opinion of the Court, the State decisions or law are not unreasonable. The opinion concludes with this statement:

> "For if we concede that in different jurisdictions different views as to the legal effect of mineral leases may be reasonably entertained, it is quite plain we think that the holding of the Texas Courts that a mineral lease is a conveyance of an interest in land is not unreasonable, but quite reasonable, and that the affixing of stamps thereon is required."

Thus the Circuit Court's opinion differs from the Treasury Department's rule requiring absolute deference to State laws only in degree, but not in principle: the taxing authorities do not assume to determine whether a decision of the highest state court upon a question within its jurisdiction is reasonable or unreasonable, whereas the Court below did assume to pass upon this question and, finding the State rule reasonable, applied it even though it differed from the general or federal law. The inevitable effect of this decision, if it were allowed to stand without challenge, is discrimination among the States and lack of uniformity in the operation of a federal taxing act intended to have nation-wide application.

CONFLICTS

1. By holding that "reasonable" rules of State law controlled the incidence of this tax, the Court below reached a decision conflicting with the decisions of this Court in *Burnet v. Harmel*, 287 U.S. 103; *Lyeth v.*

Hoey, 305 U.S. 188, and *Morgan v. Commissioner*, 309 U.S. 78. The controlling principle of all three of these decisions is that "State law may control (the incidence of a federal tax) only when the federal taxing act, by express language or necessary implication, makes its own operation dependent upon state law," and that "in the absence of language evidencing a different purpose, it (a federal taxing act) is to be interpreted so as to give a uniform application to a nation-wide scheme of taxation." In the present case it is clear that the Act, neither by express language nor necessary implication makes its operation dependent upon State law,[9] and it is equally clear that if State law is to control, it will be impossible to give uniform application to this nation-wide scheme of taxation.

In the Harmel case the question was whether an oil and gas lease on Texas land effectuated a sale of property within the purview of the Capital Gain Section[10] of the Income Tax Title of the Act. This Court, although recognizing that under Texas law the lease was a sale of capital assets, refused, for the reasons above stated, to let that fact control the operation of the capital gain section and thereby bring about a lack of

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[9]See Weil v. United States, 115 F. (2d) 999 and Niagara Hudson Power Corporation v. Hoey, Collector, 117 Fed. (2d) 414, discussed in Conflict 2, page 11, infra.

[10]By Sec. 208(a)(1) Rev. Act of 1924 (26 U. S. C. A. Sec. 939), "The term 'capital gain' means taxable gain from the sale or exchange of capital assets * * *." By Sec. 208(a) of the 1924 Act "capital assets" means property held for more than two years excluding property included in the inventory and that held for sale in the business.

uniformity in the application of a federal taxing act throughout the United States.[11]

In the *Lyeth case* the question was whether the amount received in settlement of a will contest was acquired by inheritance so as to be exempt from federal income taxation, and this Court refused to apply the Massachusetts rule (where the settlement was made) that the amount received in settlement was not acquired by inheritance, saying:

> "Whether what an heir receives from the estate of his ancestor through the compromise of his contest of his ancestor's will should be regarded as within the exemption from the federal tax should not be decided in one way in the case of an heir in Pennsylvania or Minnesota and in another way in the case of an heir in Massachusetts or New York, according to the differing views of the state courts."

In the *Morgan* case this Court refused to be governed by the Wisconsin rule as to what constituted a general power of appointment in determining the incidence of the estate tax law.

In none of these cases did this Court make any inquiry as to whether the State rule was reasonable or unreasonable, but limited its inquiry to an ascertainment of the things which Congress intended to tax or exclude from taxation. Thus the actual decision of

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[11]In other situations when called upon to construe or apply State law, this Court has not hesitated in recognizing the Texas rule that an oil and gas lease is a sale of minerals. Waggoner Estate v. Wichita County, 273 U. S. 113; Group No. 1 Oil Corporation v. Bass, 283 U. S. 279.

the Fifth Circuit, as well as its attempt to substitute for the Treasury rule requiring absolute deference to State law, a rule requiring deference to reasonable rules of State law, conflicts with the controlling decisions of this Court.

2. The decision below conflicts with recent decisions by the Second Circuit Court of Appeals, construing and applying the Stamp Tax Title of the Revenue Act of 1926, as amended, in its application to the sale and transfer of stock certificates. These cases are *Weil v. United States*, 115 Fed. (2d) 999, and *Niagara Hudson Power Corporation v. Hoey, Collector*, 117 Fed. (2d) 414. Each of these cases dealt with Treasury regulations providing that the Stamp Tax Act was inapplicable to those transfers of securities which were effected "wholly by operation of law." Which "law" —State or Federal—was not designated. In the Weil case it was shown that under New York law the transfer of corporate securities from the Mortgage Commission of the State of New York and the Superintendent of Insurance of the State of New York, as liquidator of the New York Title & Mortgage Company, to the Trustee appointed by the New York Superior Court under the Schackno Act, were "wholly by operation of law;" but the Second Circuit held, citing *Burnet v. Harmel*, that the State law could not "determine what is a taxable transfer under the United States Statute." The Niagara case involved a consolidation under which, according to the New York law, securities held by the constituent corporations passed by operation of law to the new corporation. Again the Second Circuit Court of Appeals refused to permit the incidence of the fed-

eral taxing act to be controlled by State law, citing *Burnet v. Harmel, Lyeth v. Hoey*, and its own decision in the *Weil case supra*, as requiring such a holding. Both of these opinions by the Second Circuit Court of Appeals necessarily hold that there is nothing in the Stamp Tax Title of the Revenue Act of 1926, as amended, which either expressly or by necessary implication makes its operation depend upon State law. Thus these opinions clearly conflict with the opinion below which gives controlling effect to "reasonable" rules of State Law.

3. The Court below necessarily held that Petitioner's assignments were sales within the purview of the stamp tax section. This conflicts with the decision of this Court in *Burnet v. Harmel*, 287 U.S. 103. Harmel, upon receiving large bonuses for oil and gas leases on his Texas lands, reported the bonuses as gain from the sale of capital assets taxable at a lower rate than that prevailing with respect to ordinary income. The Fifth Circuit Court of Appeals, in reliance upon the Texas rule, held that a sale had been effected. In reversing, this Court said:

> "Moreover, the statute speaks of a 'sale,' and these leases would not generally be described as a 'sale' of the mineral content of the soil, using the term either in its technical sense or as it is commonly understood."

If an oil and gas lease does not accomplish a sale of lands, tenements or other realty, then the assignment of the lessee's rights, for a consideration, is not a sale of lands, tenements or other realty.

IMPORTANT FEDERAL QUESTION NOT HERETOFORE DECIDED BY THIS COURT

This Court has never been called upon to determine the application of Section 800, Schedule A-8 of the Revenue Act of 1926, as amended by the Revenue Act of 1932, or any of the preceding statutes taxing sales of land. This Court has frequently noted the differing rules of State law with respect to the nature of an oil and gas lease and the estate or license conveyed thereby.[12] This variation in State law[13] and the Treasury's long continued practice of giving controlling effect to these varying State rules in determining the application of this schedule emphasize the importance of the question here presented and show that it should be decided by this Court.

If State law is to be given controlling effect in determining what are sales and what constitutes lands, tenements or other realty, grave questions will be raised as to whether such a construction and application results in unequal and non-uniform taxation prohibited by Article 1, Section VIII, Clause 1 of

[12]Burnet v. Harmel, supra; Ohio Oil Company v. Indiana, supra.

[13]"This type of operative act (an oil and gas lease) has been held to be a deed, a lease, a sale, a license, and an optional contract, and the legal interest created by them has been held to be a profit a prendre, a corporeal hereditament, an incorporeal hereditament, an estate in land, not an estate in land, an estate in oil and gas, not an estate in oil and gas, a servitude, a chattel real, real estate, interest in land, not an interest in land, personal property, a freehold, a tenancy at will, property interest, and the relation of landlord and tenant." Summers, Oil and Gas, Per. Ed., Vol. 1, Para. 152, p. 371, et seq.

the Constitution. Everyone must agree that from a practical standpoint the rights granted by an ordinary commercial oil and gas lease are the same throughout the United States,[14] whether those rights be called by the State Courts an interest in realty, and the lease a sale thereof, or whether they be denominated as the mere grant of a privilege to explore and capture such minerals as may be found. And the imposition of a tax upon oil leases and assignments in one State, and the deliberate failure to impose the tax upon such instruments in other States,[15] clearly brings about the lack of geographical uniformity forbidden by the Constitution and the decisions of this Court in construing it.[16] On the other hand, unless this Court decides the basic question, there will continue to be a serious doubt as to the validity of the rules which the Treasury Department has over a long period of time applied in determining the application of this schedule, and this will necessarily result in confusion and much additional litigation, which must ultimately reach this Court for decision.

The opinion of the Court below in its use of the words "transfer" and "sale" on the one hand, and "interest in realty" and "lands, tenements or other realty," on

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[14]This was conceded by the Fifth Circuit Court of Appeals, see opinion R. 59, 65; Cf. Burnet v. Harmel, supra.

[15]Oil and gas leases are subject to the Schedule A-8 documentary stamp tax, under Treasury rulings, in all of the oil and gas states except Oklahoma, West Virginia, Kansas and Louisiana (as to instruments executed prior to July 5, 1938). See Appendix, p. 27.

[16]Bromley v. McCaughn, 280 U. S. 124; Knowlton v. Moore, 178 U. S. 41.

the other, as if they were synonymous, when clearly there are vital differences between *sale* and *transfer*, and between *interest in realty* and *lands, tenements or other realty*,[17] only adds to the existing confusion and affords another reason why this Court should take jurisdiction of and decide the basic question.

CONCLUSION

Wherefore, it is respectfully submitted that this Petition for a Writ of Certiorari should be granted.

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[17]These differences, as they pertain to this case, are stated in the Appendix at page 27.